

Internal Revenue Service

Department of the Treasury
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Third Party Communication: None
Date of Communication: Not Applicable

Person To Contact:
, ID No.

Telephone Number:

Refer Reply To:
CC:CORP:B06
PLR-132529-11

Date:
February 03, 2012

Legend

Distributing =
State X =
State Y =
Business =

Date 1 =
Date 2 =
Shareholder X =
Shareholder Y =

Dear :

This letter responds to your July 28, 2011 request for rulings regarding certain federal income tax consequences of a proposed transaction. The information submitted in that request and in the later correspondence dated December 13, 2011 and January 6, 2012, is summarized below.

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination. In particular, this office has not reviewed any information pertaining to, and has made no determination regarding whether the Distribution (defined below): (i) satisfies the business purpose requirement of § 1.355-2(b); (ii) is being used principally as a device for the distribution of the earnings and profits of Distributing or Controlled or both (see § 355(a)(1)(B) of the Code and § 1.355-2(d) of the regulations); and (iii) is part of a plan (or series of related transactions) under § 355(e)(2)(A)(ii).

FACTS:

Distributing is a calendar year, State X corporation that directly conducts Business. Distributing was incorporated on Date 1 as a subchapter C corporation but converted to a subchapter S corporation effective Date 2. Financial information has been received indicating that Distributing has had gross receipts and operating expenses representing the active conduct of a trade or business for each of the past five years. Distributing has a single class of voting common stock.

Shareholder X and Shareholder Y are related. Shareholder X owns one-half of the Distributing stock. Shareholder Y owns the remaining one-half of the Distributing stock.

To avoid future disputes in the management of Business between Shareholder X and Shareholder Y and among their family members, Shareholders X and Y proposed to separate Distributing proportionally in accordance with the two families' relative share interests.

To effectuate the proposed transaction, the shareholders will cause Distributing to form a new corporation ("Controlled") and contribute to Controlled one-half of the net fair market value of the assets of Distributing solely in exchange for all of the stock of Controlled ("the Contribution"). Controlled will be formed under the laws of State X. Immediately after the transfer of assets by Distributing to Controlled, Distributing will distribute all of the stock of Controlled to Shareholder X in exchange for all of the stock of Distributing owned by Shareholder X (the "Distribution"). Controlled may elect to be taxed as a subchapter S corporation on the first available date after the Distribution.

REPRESENTATIONS:

The taxpayers have made the following representations in connection with the transaction described above.

(a) Distributing, Controlled, and each of the shareholders will each pay its or his own expenses incurred in connection with the proposed transaction.

(b) No part of the consideration to be distributed by Distributing will be received by Shareholder X as a creditor, employee, or in any capacity other than that of a shareholder of the corporation.

(c) The five years of financial information submitted on behalf of Distributing and Business is representative of the corporation's present operation, and with regard to such corporation, there have been no substantial operational changes since the date of the last financial statements submitted.

- (d) The five years of financial information submitted by Distributing on behalf of Controlled is representative of Distributing's present operations of that part of the Business, and with regard to such portion of the Business, there have been no substantial operational changes since the date of the last financial statements submitted.
- (e) Following the transaction, Distributing and Controlled will each continue the active conduct of its business, independently and with its separate employees.
- (f) The Distribution of the stock of Controlled is carried out for the following corporate business purposes: (1) The division would allow for each of the shareholders to dictate the business be run in the manner that he sees as being the most profitable; (2) to prolong the life of the corporation as it may cease operating without the separation; and (3) to allow the shareholders to decide individually their suppliers and customers. The Distribution of the stock of Controlled is motivated, in whole or substantial part, by one or more of these corporate business purposes.
- (g) The transaction is not used principally as a device for the Distribution of the earnings and profits of Distributing or Controlled or both.
- (h) There is no plan or intention to liquidate either Distributing or Controlled, to merge either corporation with any other corporation, or to sell or otherwise dispose of the assets of either corporation after the transaction, except in the ordinary course of business.
- (i) The total adjusted bases and the fair market value of the assets transferred to Controlled by Distributing will equal or exceed the sum of (i) the total liabilities (if any) assumed (within the meaning of § 357(d)) by Controlled, and (ii) the total amount of any money and the fair market value of any other property (within the meaning of § 361(b)) received by Distributing and transferred to its creditors in connection with the reorganization.
- (j) The aggregate fair market value of the assets transferred to Controlled in the Contribution will equal or exceed the aggregate adjusted basis of these assets.
- (k) Any liabilities assumed (within the meaning of § 357(d)) in the transaction and liabilities to which the transferred assets are subject were incurred in the ordinary course of business and are associated with the assets being transferred. No liabilities, including liabilities to which the transferred assets are subject, will be assumed by Controlled in the Contribution.
- (l) Distributing neither accumulated its receivables nor made extraordinary payment of its payables in anticipation of the transaction.

(m) The income tax liability for the taxable year in which investment credit property (including any building to which § 47(d) applies), if any, is transferred will be adjusted pursuant to § 50(a)(1) or (a)(2) (or § 47, as in effect before amendment by Public Law 101-508, Title 11, 104 Stat. 1388, 536 (1990), if applicable) to reflect an early disposition of the property. No investment credit has been (or will be) claimed with respect to the transferred property.

(n) No income items, including accounts receivable or any item resulting from a sale, exchange or disposition of property, that would have resulted in income to Distributing, and no items of expense will be transferred to Controlled if Distributing has earned the right to receive the income or could claim a deduction for the expense under the accrual or similar method of accounting.

(o) No intercorporate debt will exist between Distributing and Controlled at the time of, or subsequent to, the Distribution.

(p) Payments made in connection with all continuing transactions, if any, between Distributing and Controlled, will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.

(q) No two parties to the transaction are investment companies as defined in § 368(a)(2)(F)(iii) and (iv).

(r) The Distribution is not part of a plan or series of related transactions (within the meaning of § 1.355-7) pursuant to which one or more persons will acquire directly or indirectly stock representing a 50 percent or greater interest (within the meaning of § 355(d)(4)) in Distributing or Controlled (including any predecessor or successor of any such corporation).

(s) For purposes of § 355(d), immediately after the Distribution, no person (determined after applying § 355(d)(7)) will hold stock possessing 50 percent or more of the total combined voting power of all classes of Distributing stock entitled to vote, or 50 percent or more of the total value of shares of all classes of Distributing stock, that was acquired by purchase (as defined in § 355(d)(5) and (8)) during the five-year period (determined after applying § 355(d)(6)) ending on the date of the Distribution.

(t) For purposes of § 355(d), immediately after the Distribution, no person (determined after applying § 355(d)(7)) will hold stock possessing 50 percent or more of the total combined voting power of all classes of Controlled stock, or 50 percent or more of the value of the total combined shares of all classes of Controlled stock, that was either (i) acquired by purchase (as defined in § 355(d)(5) and (8)) during the five-year period (determined after applying § 355(d)(6)) ending on the date of the Distribution, or (ii) attributable to distributions on Distributing stock that was acquired by purchase (as defined in § 355(d)(5) and (8)) during the five-year period (determined after applying

§ 355(d)(6)) ending on the date of the Distribution.

(u) The fair market value of Controlled stock and other consideration to be received by Shareholder X will be approximately equal to the fair market value of Distributing stock surrendered by Shareholder X in the exchange.

(v) The total fair market value of the assets transferred in the proposed transaction will equal or exceed the aggregate adjusted bases of those assets.

(w) Immediately after the Distribution, neither Distributing nor Controlled will be a disqualified investment corporation (within the meaning of § 355(g)(2)).

(x) Distributing is an S corporation (within the meaning of § 1361 (a)). Controlled will elect to be an S corporation pursuant to § 1362 (a) on the first available date after the Distribution and there is no plan or intent to revoke or otherwise terminate the S corporation election of either Distributing or Controlled.

RULINGS:

Based solely on the information submitted and on the representations set forth above, we rule as follows with respect to the proposed transaction.

(1) The transfer by Distributing to Controlled of part of its assets in exchange for all of Controlled stock in the Contribution, followed by the Distribution of all Controlled stock to Shareholder X in exchange for all Distributing stock held by Shareholder X, will constitute a reorganization within the meaning of § 368(a)(1)(D). Distributing and Controlled will each be "a party to a reorganization" within the meaning of § 368(b).

(2) No gain or loss will be recognized by Distributing on the Contribution. (§§ 361(a) & 357(a)).

(3) No gain or loss will be recognized by Controlled on the Contribution. (§ 1032(a)).

(4) No gain or loss will be recognized by Distributing on the Distribution to Shareholder X of the stock of Controlled in exchange for all Distributing stock held by Shareholder X. (§361(c)(1)).

(5) The basis in each asset received by Controlled from Distributing in the Contribution will be the same as the basis of such asset in the hands of Distributing immediately prior to the transaction. (§ 362(b)).

(6) The holding period of each asset transferred to Controlled from Distributing in the Contribution will include the period during which such asset was held by Distributing. (§ 1223(2)).

(7) No gain or loss will be recognized by (and no amount will otherwise be included in the income of) Shareholder X upon the receipt of the stock of Controlled in exchange for the stock of Distributing held by Shareholder X. (§ 355(a)(1)).

(8) The aggregate basis of the stock of Controlled in the hands of Shareholder X will be the same as the aggregate basis of the stock of Distributing surrendered by Shareholder X in exchange therefore. (§ 358(a)).

(9) The holding period of the stock of Controlled received by Shareholder X will include the holding period of the stock of Distributing surrendered by Shareholder X in exchange therefore, provided such stock is held as a capital asset on the date of the transaction. (§ 1223(1)).

(10) Following the Distribution of the stock of Controlled, proper allocation of earnings and profits will be made between Distributing and Controlled in accordance with Treas. Reg. Section 1.312-10(a).

(11) Distributing's momentary ownership of the stock of Controlled, as part of the reorganization under section 368(a)(1)(D), will not cause Controlled to have an ineligible shareholder for any portion of its first taxable year under section 1361(b)(1)(B).

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. In particular, no opinion is expressed regarding: (i) whether the Distribution satisfies the business purpose requirement of § 1.355-2(b); (ii) whether the Distribution is used principally as a device for the distribution of the earnings and profits of Distributing or Controlled or both (see § 355(a)(1)(B) of the Code and § 1.355-2(d) of the regulations); and (iii) whether the Distribution is part of a plan (or series of related transactions) under § 355(e)(2)(A)(ii). Furthermore, no opinion is expressed as to the validity of any S corporation election of either Distributing or Controlled.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of the letter ruling.

Sincerely,

Mary E. Goode
Mary E. Goode
Senior Counsel, Branch 6
(Corporate)